

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**(A Component Unit of the State of North Dakota)**

***FINANCIAL STATEMENTS***  
***DECEMBER 31, 2004 AND 2003***

## **NORTH DAKOTA MUNICIPAL BOND BANK**

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## INDEPENDENT AUDITOR'S REPORT

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

We have audited the accompanying basic financial statements of the **North Dakota Municipal Bond Bank**, a component unit of the State of North Dakota, as of and for the years ended December 31, 2004 and 2003, as listed in the table of contents. These financial statements are the responsibility of the Bond Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the **North Dakota Municipal Bond Bank** as of December 31, 2004 and 2003, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 26, 2005 on our consideration of **North Dakota Municipal Bond Bank's** internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

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The Management's Discussion and Analysis on pages 3 through 6 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the **North Dakota Municipal Bond Bank**. The accompanying supplemental information on pages 28 through 31 are presented for purpose of additional analysis and are not a required part of the basic financial statements of the **North Dakota Municipal Bond Bank**. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Eide Bailly LLP*

Bismarck, North Dakota  
January 26, 2005

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**DECEMBER 31, 2004 AND 2003**  
**(In Thousands)**

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The discussion and analysis of the financial performance of the North Dakota Municipal Bond Bank (Bond Bank) that follows is meant to provide additional insight into the Bond Bank's activities for the years ended December 31, 2004 and 2003. Please read it in conjunction with the Bond Bank's financial statements and footnotes, which are presented within this report.

**FINANCIAL HIGHLIGHTS:**

Municipal securities (loans outstanding) increased from \$194,645 in 2003 to \$198,631 in 2004. SRF loans are funded with grant revenues and bond proceeds, which are invested until loans are funded. Grant revenues decreased by \$7,838 as available bond proceeds, rather than grants, were utilized to fund numerous loan requests. Also, there were no large refinancings funded in 2004. In 2003, there were \$31,003 of SRF loans funded as compared to \$15,516 in 2004. The Bond Bank anticipates loan demand will continue to remain strong as political subdivisions work to achieve compliance with the Environmental Protection Agency's (EPA) Drinking Water regulations.

The Bond Bank's rebate due to the Internal Revenue Service increased by \$138. There were no rebate payments made to the IRS in 2004. In 2003, rebate payments totaling \$822 were made to the IRS. As of year-end, the Series 1995A and 2000A SRF bonds' respective ten-year and five-year rebate payments totaling \$110 of the rebate liability are considered current.

The Bond Bank issued \$880 of bonds under its Capital Financing Program (rated A- by Standard & Poor's) in 2004. In 2003, \$1,495 of bonds was issued under this program. The State Revolving Fund Loan Program (rated Aaa by Moody's) issues bonds to provide the required match to receive capitalization grants from the EPA. The Bond Bank issued \$11,790 of SRF Series 2004A bonds. The proceeds of the SRF Series 2004A were used to partially refund SRF Series 2000A bonds. The Bond Bank issued \$47,250 of SRF bonds in 2003. The Bond Bank anticipates issuing State Revolving Fund Program bonds in 2005 to provide match for future capitalization grants. There were no rating changes to either program in 2004.

The growing State Revolving Fund Program helped the Bond Bank's total assets increase \$8,706 to \$339,404. The balance sheet indicates that the Bond Bank continues to have adequate resources to provide for bond repayments. Change in net assets of the Bond Bank resulted in an increase of \$16,681 providing the Bond Bank with an overall strong financial position. Grant proceeds account for a significant portion of net assets. Federal law provides that grants may only be expended for SRF program purposes. Net assets are also restricted for debt service of bond issues or for the purchase of municipal securities. As of December 31, 2004, the Bond Bank had \$41,229 of commitments to extend credit.

**REQUIRED FINANCIAL STATEMENTS:**

The discussion and analysis are intended to serve as an introduction to the Bond Bank's financial statements. The financial statements of the Bond Bank provide accounting information similar to that of many other business entities. The Balance Sheets summarize the assets and liabilities, with the difference between the two reported as net assets. It also serves as the basis for analysis of the soundness and liquidity of the Bond Bank. The Statements of Revenues, Expenses and Changes in Fund Net Assets summarize the Bond Bank's operating performance for the two years. The Statements of Cash Flows summarizes the flow of cash through the Bond Bank as it conducts its business.

CONDENSED BALANCE SHEETS  
DECEMBER 31,

	2004	2003
<b>ASSETS</b>		
CURRENT ASSETS - UNRESTRICTED	\$ 2,566	\$ 2,429
CURRENT ASSETS - RESTRICTED	20,169	21,373
NONCURRENT ASSETS - RESTRICTED	316,670	306,892
TOTAL ASSETS	<u>\$ 339,405</u>	<u>\$ 330,694</u>
<b>LIABILITIES</b>		
CURRENT LIABILITIES	\$ 10,927	\$ 9,253
NONCURRENT LIABILITIES	148,402	158,045
TOTAL LIABILITIES	<u>159,329</u>	<u>167,298</u>
<b>NET ASSETS</b>		
UNRESTRICTED	2,556	2,424
RESTRICTED FOR DEBT SERVICE	89,737	71,638
RESTRICTED FOR LOAN PURPOSES	87,783	89,334
TOTAL NET ASSETS	<u>180,076</u>	<u>163,396</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 339,405</u>	<u>\$ 330,694</u>

*Cash and Investments*

Certain Bond Bank cash and investments, which are included in the restricted current and noncurrent assets, are restricted for the debt service of bond issues or for the purchase of municipal securities. Additional discussion of these investments can be found at Note 3 to the financial statements.

*Municipal Securities*

Obligations of North Dakota political subdivisions are classified separately on the balance sheet as "municipal securities" and included in the restricted current and noncurrent assets of the condensed Balance Sheet. These investment securities are primarily city, school district and water district obligations and are pledged to the various bond issues. No losses for market value declines are anticipated and an allowance has not been provided. Note 3 to the financial statements contain further information regarding municipal securities.

**MANAGEMENT'S DISCUSSION AND ANALYSIS – page 3**  
**(In Thousands)**

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*Bonds Payable*

In order to provide local political subdivisions with funds to finance projects, the Bond Bank has issued bonds to facilitate the purchase of the political subdivision's municipal securities. The bonds payable are included in the restricted current and noncurrent liabilities of the preceding statement. The bonds are direct obligations of the Bond Bank and are secured by municipal securities purchased under the applicable resolutions, interest earnings and certain accounts established pursuant to the applicable bond resolutions. Further details are contained in Note 4 to the financial statements.

*Rebate Due to IRS*

Under Internal Revenue Service Code Sections 103 and 148, earnings from nonpurpose investments in excess of bond interest expense must be remitted as a rebate, once every five years, to the U.S. Treasury. This liability is included in the noncurrent liabilities. Note 8 to the financial statements contain additional information.

**CONDENSED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS**  
**YEARS ENDED DECEMBER 31,**

	<u>2004</u>	<u>2003</u>
OPERATING REVENUES		
Investment income	\$ 6,120	\$ 6,193
Administrative fees and other	916	984
	<u>7,036</u>	<u>7,177</u>
NONOPERATING REVENUE		
Grant and set-asides	11,414	19,250
Investment income	7,481	6,662
	<u>18,895</u>	<u>25,912</u>
TOTAL REVENUE	<u>25,931</u>	<u>33,089</u>
OPERATING EXPENSES		
Interest expense	7,926	7,831
State Revolving Fund expenses	883	1,014
Rebate due to IRS	137	211
Amortization of bond issue costs	153	133
Other	152	159
	<u>9,251</u>	<u>9,348</u>
CHANGE IN NET ASSETS	16,680	23,741
TOTAL NET ASSETS, BEGINNING OF YEAR	<u>163,396</u>	<u>139,655</u>
TOTAL NET ASSETS, END OF YEAR	<u>\$ 180,076</u>	<u>\$ 163,396</u>

Note 1 to the financial statements contains discussion of several of the various operating revenue and expense items pertaining to Bond Bank operations.

*Grant and set-asides*

Under an agreement with the North Dakota Department of Health, the Bond Bank assists in administering the State Revolving Loan Fund. The grant proceeds are classified as nonoperating revenue in the Statement of Revenues, Expenditures and Changes in Net Assets.

The purpose of the Loan Fund is to provide low cost financing to local political subdivisions to finance wastewater disposal system projects and drinking water projects. The federal Environmental Protection Agency (EPA) provides funds to finance approximately 80 percent of the cost of the projects. The state finances its 20 percent share of the cost through bonds issued by the Bond Bank.

*Economic Factors and Budgetary Information*

Note 1 to the financial statements discusses the Bond Bank's economic dependence on North Dakota political subdivision municipal securities obligations.

As discussed in financial statement Note 1, the Bond Bank, an agency of the Industrial Commission, operates through a biennial appropriation provided by the State Legislature. The Bond Bank prepares a biennial budget as a part of the Industrial Commission's budget, which is included in the Governor's budget that is presented to the General Assembly at the beginning of each legislative session. The Bond Bank has a continuous appropriation of income from operations. Changes to the appropriation not falling under the continuing appropriation are subject to approval by the State Emergency Commission.

*Contacting the North Dakota Municipal Bond Bank's financial management:*

The information in this report is intended to provide the reader with an overview of the Bond Bank's operations along with the Bond Bank's accountability for those operations. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the North Dakota Municipal Bond Bank, PO Box 5509, Bismarck, ND 58506-5509.



**NORTH DAKOTA MUNICIPAL BOND BANK**  
**BALANCE SHEETS**  
**DECEMBER 31, 2004 AND 2003**  
**(In Thousands)**

	<u>2004</u>	<u>2003</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents - unrestricted	\$ 2,566	\$ 2,429
Restricted		
Restricted cash and cash equivalents	1,602	1,781
Interest receivable	3,404	3,352
Investments	5,634	4,491
Municipal securities	9,529	11,749
Total restricted current assets	<u>20,169</u>	<u>21,373</u>
Total current assets	<u>22,735</u>	<u>23,802</u>
<b>NONCURRENT ASSETS - RESTRICTED</b>		
Investments	119,679	116,133
Municipal securities	189,692	182,896
Deferred bond financing costs, net	1,246	1,403
Advance to Bank of North Dakota	6,053	6,460
Total restricted noncurrent assets	<u>316,670</u>	<u>306,892</u>
Total assets	<u>\$ 339,405</u>	<u>\$ 330,694</u>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 33	\$ 60
Rebate due to IRS	110	-
Bonds payable	9,150	7,625
Interest payable	1,634	1,568
Total current liabilities	<u>10,927</u>	<u>9,253</u>
<b>NONCURRENT LIABILITIES</b>		
Rebate due to IRS	338	309
Bonds payable, net	142,011	151,276
Advance from Bank of North Dakota	6,053	6,460
Total noncurrent liabilities	<u>148,402</u>	<u>158,045</u>
Total liabilities	<u>159,329</u>	<u>167,298</u>
<b>NET ASSETS</b>		
Unrestricted	2,556	2,424
Restricted for debt service	89,737	71,638
Restricted for loan purposes	87,783	89,334
Total net assets	<u>180,076</u>	<u>163,396</u>
Total liabilities and net assets	<u>\$ 339,405</u>	<u>\$ 330,694</u>

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS**  
**YEARS ENDED DECEMBER 31, 2004 AND 2003**  
(In Thousands)

	<u>2004</u>	<u>2003</u>
OPERATING REVENUES		
Investment income	\$ 6,120	\$ 6,193
Administrative fees and other	916	984
	<u>7,036</u>	<u>7,177</u>
OPERATING EXPENSES		
Interest expense	7,926	7,831
State Revolving Fund administration	488	487
State Revolving Fund set-asides	395	527
Rebate due to IRS	137	211
Salaries and benefits	112	115
Amortization of bond issue costs	153	133
Operating	31	35
Paying agent fees	9	9
	<u>9,251</u>	<u>9,348</u>
OPERATING LOSS	<u>(2,215)</u>	<u>(2,171)</u>
NONOPERATING REVENUE		
Grant and set-asides	11,414	19,250
Investment income	7,481	6,662
	<u>18,895</u>	<u>25,912</u>
CHANGE IN NET ASSETS	16,680	23,741
TOTAL NET ASSETS, BEGINNING OF YEAR	<u>163,396</u>	<u>139,655</u>
TOTAL NET ASSETS, END OF YEAR	<u>\$ 180,076</u>	<u>\$ 163,396</u>

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**STATEMENTS OF CASH FLOWS**  
**YEARS ENDED DECEMBER 31, 2004 AND 2003**  
(In Thousands)

	<u>2004</u>	<u>2003</u>
<b>OPERATING ACTIVITIES</b>		
Receipts of administrative fees from customers	\$ 917	\$ 984
Payments to service providers	(952)	(1,029)
Payments to employees	(112)	(115)
Payment of rebate to IRS	-	(822)
<b>NET CASH USED FOR OPERATING ACTIVITIES</b>	<u>(147)</u>	<u>(982)</u>
<b>NONCAPITAL FINANCING ACTIVITIES</b>		
Grant and set-asides	11,414	19,250
Interest paid on bonds payable	(7,544)	(7,786)
Bond financing costs	(124)	(441)
Principal payment on advance from Bank of North Dakota	(407)	(1,041)
Proceeds from bond premiums	509	2,889
Proceeds from issuance of bonds payable	12,670	48,745
Principal payments on bonds payable	(21,106)	(31,619)
<b>NET CASH FROM (USED FOR) NONCAPITAL FINANCING ACTIVITIES</b>	<u>(4,588)</u>	<u>29,997</u>
<b>INVESTING ACTIVITIES</b>		
Interest received on investments and municipal securities	13,551	12,481
Collection of advance to Bank of North Dakota	407	1,041
Proceeds from maturities and sales of investments	38,809	65,292
Purchases of investments	(44,088)	(88,837)
Proceeds from maturities of municipal securities	12,416	11,763
Purchases of municipal securities	(16,402)	(32,257)
<b>NET CASH FROM (USED FOR) INVESTING ACTIVITIES</b>	<u>4,693</u>	<u>(30,517)</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<u>(42)</u>	<u>(1,502)</u>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<u>4,210</u>	<u>5,712</u>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<u>\$ 4,168</u>	<u>\$ 4,210</u>
<b>CASH AND CASH EQUIVALENTS - UNRESTRICTED</b>	<u>\$ 2,566</u>	<u>\$ 2,429</u>
<b>RESTRICTED CASH AND CASH EQUIVALENTS</b>	<u>1,602</u>	<u>1,781</u>
<b>TOTAL CASH AND CASH EQUIVALENTS</b>	<u>\$ 4,168</u>	<u>\$ 4,210</u>

**STATEMENTS OF CASH FLOWS – page 2**  
**(In Thousands)**

	<u>2004</u>	<u>2003</u>
RECONCILIATION OF OPERATING LOSS TO TO NET CASH USED FOR OPERATING ACTIVITIES		
Operating loss	\$ (2,215)	\$ (2,171)
Adjustments to reconcile operating loss to net cash used for operating activities		
Amortization of bond financing costs	153	133
Net accretion of discount on bonds payable	(750)	743
Reclassification of investment income and expense to other activities	2,554	895
Changes in assets and liabilities		
Accounts payable	(28)	29
Rebate due IRS	139	(611)
NET CASH USED FOR OPERATING ACTIVITIES	<u>\$ (147)</u>	<u>\$ (982)</u>

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**STATEMENT OF APPROPRIATIONS**  
**TWO YEARS ENDED JUNE 30, 2003 AND EIGHTEEN MONTHS ENDED DECEMBER 31, 2004**  
(In Thousands)

Note: Only appropriations of specific amounts are included in this statement. A reconciliation to the operating expenses on the December 31, 2004 and 2003 statement of revenues and expenses follows:

	2001-2003	7-1-01- 12-31-01 Expenditures	1-1-02- 12-31-02 Expenditures	1-1-03- 6-30-03 Expenditures	Unexpended Appropriations at 6-30-03	2003-2005 Appropriations	7-1-03- 12-31-03 Expenditures	Unexpended Appropriations at 12-31-03	1-1-04- 12-31-04 Expenditures	Unexpended Appropriations at 12-31-04
Salaries and wages	\$ 375	\$ 59	\$ 111	\$ 57	\$ 148	\$ 311	\$ 57	\$ 254	\$ 112	\$ 142
Operating expenses	283	21	37	26	199	243	10	233	31	202
Total administrative expenses	658	80	148	83	347	554	67	487	143	344
Equipment	13	-	-	-	13	12	-	12	-	12
Total expenses	\$ 671	\$ 80	\$ 148	\$ 83	\$ 360	\$ 566	\$ 67	\$ 499	\$ 143	\$ 356
<b>2004</b>										
<b>2003</b>										
Total appropriation expenditures for year ended December 31	\$ 143	\$ 150								
Interest expense	7,925	7,831								
Depreciation and amortization	153	133								
State Revolving Fund administrative fees	882	1,014								
Rebate due to IRS	138	211								
Administrative and operating expenses paid out of general operating funds - paying agent fees	10	9								
Total operating expenses	\$ 9,251	\$ 9,348								

See Notes to Financial Statements

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2004 AND 2003**  
**(In Thousands)**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES**

*Nature of Operations*

The North Dakota Municipal Bond Bank (Bond Bank) was established July 1, 1975, by the North Dakota Legislature, as provided in Chapter 6-09.4 of the North Dakota Century Code, as a separate agency of the State of North Dakota. The purpose of the Bond Bank is to make funds available for borrowing by North Dakota political subdivisions through the issuance of its bonds and the purchase of municipal securities of the political subdivisions. The Bond Bank has been granted all powers required in order to accomplish this purpose and is under the control and management of the North Dakota Industrial Commission.

*Reporting Entity*

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, the Bond Bank should include all component units over which the Bond Bank exercises such aspects as (1) appointing a voting majority of an organization's governing body and (2) has the ability to impose its will on that organization, or (3) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Bond Bank. GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, an Amendment of GASB Statement 14, further defined reporting units as a legally separate, tax exempt affiliated organization that meet all of the following criteria:

- The economic resources of the organization entirely or almost entirely directly benefit the Bond Bank or its constituents, and
- The Bond Bank or its component units are entitled to or can otherwise access, a majority of the economic resources of the organization, and
- The economic resources that the Bond Bank is entitled to, or can otherwise access, are significant to the Bond Bank.

Based on the criteria of GASB Statement No. 14 and 39, no organizations were determined to be part of the reporting entity. The Bond Bank is included as a discretely presented component unit within the State of North Dakota's reporting entity.

*Budgetary Process*

The Bond Bank operates through a biennial appropriation provided by the State Legislature. The Bond Bank prepares a biennial budget which is included in the Governor's budget that is presented to the General Assembly at the beginning of each legislative session. The General Assembly enacts the budgets of the various state departments through passage of specific appropriation bills. The Governor has line item veto powers over all legislation subject to legislative override. Once passed and signed, the appropriation becomes the Bond Bank's financial plan for the next two years. The Bond Bank has a continuous appropriation of income from operations. Changes to the appropriation not falling under the continuing appropriation are subject to approval by the State Emergency Commission.

The Statement of Appropriations has been prepared using the accrual basis of accounting and includes only those expenses for which an appropriation has been established.

## NOTES TO FINANCIAL STATEMENTS

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### *Basis of Accounting and Measurement Focus*

The North Dakota Municipal Bond Bank is presented in the accompanying financial statements as a proprietary fund type - an enterprise fund.

An enterprise fund is used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent is that costs of providing goods or services to the general public or other funds on a continuing basis be financed or recovered primarily through user charges. The Bond Bank recovers its costs through administrative charges to municipalities and earnings on administrative funds. The Program revenues include 1) Income from receivables and 2) Administrative fees. The Non Program revenues include 1) Investment income and 2) Income from grants and set-asides.

As a proprietary fund type, the Bond Bank accounts for its transactions using the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

The accompanying financial statements of the North Dakota Municipal Bond Bank follow the pronouncements of the Governmental Accounting Standards Board (GASB), which is the nationally accepted standard-setting body for establishing generally accepted accounting principles for governmental entities. In accordance with Governmental Accounting Standards Board Statement No. 20, the Bond Bank follows all applicable GASB Pronouncements as well as following Financial Accounting Standards Board pronouncements issued on or before November 30, 1989 unless those pronouncements conflict with GASB pronouncements.

### *Use of Estimates*

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect reported amounts of assets and liabilities at the date of the balance sheet and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

### *Concentration of Credit Risk*

Municipal securities primarily consist of obligations of cities, school districts and water organizations. The Bond Bank performs credit evaluations and, in some instances, municipal securities are collateralized by property and leases. Generally, the Bond Bank maintains a security interest until related receivables are collected. Municipal securities are due under terms corresponding with applicable bonds. All customers are located in the state of North Dakota.

## NOTES TO FINANCIAL STATEMENTS

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### *Cash and Cash Equivalents*

The Bond Bank considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. The Bond Bank follows the bond indenture documentation on satisfying requirements for unrestricted and restricted cash and cash equivalents.

### *Investments*

Investments are reported at fair value. All investment income, including changes in the fair value of investments, is recognized in the statement of revenues, expenses, and changes in fund net assets. A portion of the Bond Bank's investments consists of nonparticipating contracts. These instruments are reported at cost. The Bond Bank follows the bond indenture documentation on satisfying requirements for unrestricted and restricted investments.

Funds held by trustees or the Bond Bank under bond resolutions is to be invested to the fullest extent possible in investment obligations selected by the Bond Bank. The maturity date or the date on which such investment obligations may be redeemed shall coincide as nearly as practicable with the date or dates on which moneys in the funds or accounts for which the investments were made will be required. The restricted bond accounts have their moneys invested in various debt securities such as U.S. Treasury securities, U.S. Government Agency securities, tax-exempt obligations of states and political subdivisions, certificates of deposit, and investment contracts.

### *Deferred Bond Financing Costs*

Bond issuance costs are being amortized over the life of the bonds using the interest method.

### *Equipment and Furnishings*

Equipment and furnishings are stated at cost, net of accumulated depreciation. Equipment and furnishings with a cost of \$5,000 or more per unit are capitalized and reported in the accompanying financial statements. Depreciation is computed using the straight-line method over the estimated useful lives of the assets which range from five to ten years.

### *Accumulated Unpaid Vacation and Sick Pay*

Annual leave and sick leave are a part of permanent employees' compensation as set forth in Section 54-06-14 of the North Dakota Century Code. Annual leave is earned based on tenure of employment, within a range of a minimum of one working day per month of employment, to a maximum of two working days per month of employment, to be fixed by rules and regulations adopted by the employing unit. In general, accrued annual leave cannot exceed 30 days at each year-end, as set by the Agency. Employees are paid for unused annual leave upon termination or retirement.

Sick leave is earned based on tenure at the rate of one working day per month of employment. There are no limitations on the amount of sick leave that an employee can accumulate. Employees who have ten continuous years of service are paid one-tenth of their accumulated sick leave upon leaving service under chapter 54-52 of the North Dakota Century Code.

Vacation and sick leave are immaterial as of December 31, 2004 and 2003, and are not accrued.



## NOTES TO FINANCIAL STATEMENTS

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### *Restricted Net Assets*

The Bond Bank administers the SRF federal grant programs for the North Dakota Department of Health. Grant proceeds account for a significant portion of net assets. Federal law provides that the grants may only be expended for SRF program purposes. Net assets are also restricted for debt service of bond issues or for the purchase of municipal securities. The Bond Bank follows the CFP and SRF bond indenture for the repayment of restricted net assets.

### *Operating and Non-operating Revenues*

Operating revenues consist of sales of goods and services, quasi-external operating transactions with other funds, grant revenue for specific activities that are considered to be operating activities of the grantor, receipts from other agencies for reimbursement of operating transactions and other miscellaneous revenue. Grants that would qualify as an operating activity are those that do not subsidize an existing program, rather they finance a program the agency would not otherwise undertake.

All other revenues that do not meet the above criteria are classified as non-operating.

### *Administrative Fee Revenue*

All loans originated by the Bond Bank are charged an administration fee. These fees are used to cover the costs incurred in the administration of the loan programs. Income is recorded when the fees are received.

### *Grant and Set-Asides Revenue*

The SRF Program grants, received from the United States Environmental Protection Agency, are to be used to make below-market interest rate loans to political subdivisions for the purpose of financing authorized projects. In addition, the Drinking Water SRF Program is allowed to "set-aside" a percentage of each grant award, which is expended for administration, technical assistance and source water assessment programs.

### *State Revolving Fund Administration Expense*

State Revolving Fund administration expenses are incurred by the Bond Bank and North Dakota Department of Health in administration of the State Revolving Loan Programs.

### *State Revolving Fund Set-Asides Expenses*

The Drinking Water SRF Program is allowed to "set-aside" a percentage of each grant award, which is expended for administration, technical assistance and source water assessment programs.

### *Rebate Due to IRS*

Under Internal Revenue Service Code Sections 103 and 148, earnings from nonpurpose investments in excess of bond interest expense must be remitted as rebate, once every five years, to the U.S. Treasury. Annually, rebate is calculated and the liability is accordingly adjusted.

## NOTES TO FINANCIAL STATEMENTS

### NOTE 2 - DEPOSITS AND INVESTMENTS

#### DEPOSITS

The North Dakota Municipal Bond Bank is required to maintain its deposits at the Bank of North Dakota. As of December 31, 2004, the Bond Bank had the following deposits (amounts in the thousands):

	<b>Bank Balance</b>	<b>Less Than 1 Year</b>	<b>1-5 Years</b>	<b>6-10 Years</b>	<b>More Than 10 years</b>
Cash and cash equivalents	\$ 4,168	\$ 4,168	\$ -	\$ -	\$ -
Certificates of deposit	6,220	5,676	-	544	-
Certificates of deposit recorded as advances to Bank of North Dakota	6,053	-	750	2,768	2,535
Bank investment contracts - Bank of North Dakota	11,478	-	-	-	11,478
Canadian Imperial Bank of Commerce	9,044	-	-	9,044	-
Total deposits	<u>\$ 36,963</u>	<u>\$ 9,844</u>	<u>\$ 750</u>	<u>\$ 12,356</u>	<u>\$ 14,013</u>

#### *Custodial and Concentration Credit Risk*

For a deposit, the custodial credit risk that, in the event of the failure of a depository financial institution, the Bond Bank will not be able to recover collateral securities that are in the possession of an outside party. The Bond Bank's deposits are uncollateralized. All of the deposits, except Canadian Imperial Bank of Commerce, are with the Bank of North Dakota.

#### INVESTMENTS

NDCC 6-09.4-7 authorizes the Bond Bank to invest any funds in the same manner as permitted for investment of funds belonging to the state or the Bank of North Dakota. The Bond Bank does not have a formal investment policy. The General Bond Resolution and Master Trust Indenture specify the permitted investments. The Bond Bank follows those stipulations when investing funds.

Funds held by trustees or the Bond Bank under bond resolutions are to be invested to the fullest extent possible in investment obligations selected by the Bond Bank. The maturity date or the date on which such investment obligations may be redeemed shall coincide as nearly as practicable with the date or dates on which moneys in the funds or accounts for which the investments were made will be required. The restricted bond accounts may have their moneys invested in various debt securities such as U.S. Treasury securities, U.S. Government Agency securities, guaranteed investment contracts and certificates of deposit. There is no limit on the amount the Bond Bank may invest in any one issuer.

## NOTES TO FINANCIAL STATEMENTS

As of December 31, 2004, the Bond Bank had the following investments and maturities (amounts are in thousands):

	<b>Fair Value</b>	<b>Less Than 1 Year</b>	<b>1-5 Years</b>	<b>6-10 Years</b>	<b>More Than 10 years</b>
MBIA	\$ 39,900	\$ -	\$ -	\$ -	\$ 39,900
IXIS Funding Corp.	17,792	-	-	-	17,792
GE Funding	20,437	-	-	-	20,437
Trinity Plus Funding Company	20,362	-	-	-	20,362
US Treasuries	80	10	55	15	-
Total guaranteed investment contracts	<u>\$ 98,571</u>	<u>\$ 10</u>	<u>\$ 55</u>	<u>\$ 15</u>	<u>\$ 98,491</u>

### *Credit Risk*

The Bond Bank's North Dakota State Revolving Fund Program Master Trust Indenture restricts investments in Guaranteed Investment Contracts (GICs) and Bank Investment Contracts (BICs) issued, at the time the contract is entered into, a long-term debt rating by Moody's, at least equal to the better of (i) "A" or (ii) the then current rating assigned by Moody's to the Bonds without regard to credit enhancement for long-term obligations.

### *Concentration of Credit Risk*

Each of the above listed investments represent 5 percent or more of total investments.

## NOTE 3 - MUNICIPAL SECURITIES

Obligations of North Dakota political subdivisions are classified separately on the balance sheet as "municipal securities." These investment securities are primarily obligations of cities, school districts and water organizations, and are pledged to the various bond issues. Due to the maturity of these securities, a market value is not readily available. The Bond Bank intends to hold these securities to maturity. No losses for market value decline is anticipated and an allowance has not been provided. The Bond Bank had the following municipal securities as of December 31:

	<b>2004</b>	<b>2003</b>
Capital financing program	\$ 29,976	\$ 31,454
State revolving fund program	169,245	163,191
	<u>199,221</u>	<u>194,645</u>
Less current portion	9,529	11,749
	<u>\$ 189,692</u>	<u>\$ 182,896</u>

## NOTES TO FINANCIAL STATEMENTS

### NOTE 4 - BONDS PAYABLE

#### *Changes in Bonds Payable*

The following is a summary of changes in bonds payable for the years ended December 31, 2004 and 2003:

Balance, December 31, 2002	\$ 138,903
Issuance of bonds payable	48,745
Principal payments on bonds payable	(29,490)
Net accretion of premiums and discounts on bonds payable	743
Balance, December 31, 2003	158,901
Issuance of bonds payable	12,670
Principal payments on bonds payable	(19,660)
Net accretion of premiums and discounts on bonds payable	(751)
Balance, December 31, 2004	\$ 151,160

#### *Bonds Payable*

The bonds of the Bond Bank have been issued to provide financing to purchase municipal securities in order to provide local political subdivisions with funds to finance local projects. The bonds are direct obligations of the Bond Bank and are secured by municipal securities purchased under the applicable resolutions, interest earnings and certain accounts established pursuant to the applicable bond resolutions.

#### *Maturities of Bonds Payable*

Maturities of principal and interest on all bonds are as follows:

Years Ending December 31,	Principal	Interest	Total Debt Service
2005	\$ 9,150	\$ 7,228	\$ 16,378
2006	9,520	6,753	16,273
2007	9,840	6,258	16,098
2008	10,020	5,788	15,808
2009	10,385	5,325	15,710
2010-2014	50,835	19,760	70,595
2015-2019	38,730	8,518	47,248
2020-2024	12,740	1,488	14,228
2025-2028	615	70	685
Discounts, net of premiums	(675)	675	-
	\$ 151,160	\$ 61,863	\$ 213,023

## NOTES TO FINANCIAL STATEMENTS

The following summarizes the Bond Bank's bonds outstanding at December 31, 2004 and 2003:

<b>Description and Due Date</b>	<b>Interest Rate</b>	<b>Original Value</b>	<b>2004</b>	<b>2003</b>
Series 1990-CFP Serial Bonds 12/1/03-12/1/05	7.30-7.40	\$ 3,750	\$ 25	\$ 45
Series 1991-CFP Serial Bonds 12/1/03-12/1/06	6.25	6,225	20	25
Series 1992-CFP Serial Bonds 6/1/03-6/1/07	6.50	13,535	15	135
Series 1993-CFP Serial Bonds 6/1/03-6/1/13	4.50-5.75	7,905	2,795	3,250
Series 1993-SRF Serial Bonds 10/1/03-10/1/14 (net of discount)	5.55-6.25	20,220	4,172	5,076
Series 1994-CFP Serial Bonds - 6/1/03-6/1/04	5.70	6,305	-	145
Series 1995-CFP Serial Bonds 6/1/03-6/1/15	5.00-6.00	2,505	1,205	1,305
Series 1995-SRF Serial Bonds 10/1/03-10/1/07 (net of discount)	5.80-6.40	6,975	978	1,269
Series 1996-CFP Serial Bonds 6/1/03-6/1/16	5.10-6.60	3,365	665	775
Series 1996-SRF Serial Bonds 10/1/03-10/1/17 (net of premium)	5.10-6.00	29,845	3,066	4,237
Series 1997-CFP Serial Bonds 6/1/03-6/1/17	4.60-7.15	15,345	7,380	7,895
Series 1998-CFP Serial Bonds 6/1/03-6/1/23 (net of deferred loss on refunding of \$134)	4.15-5.25	9,695	5,501	6,129
Series 1998-SRF Serial Bonds 10/1/03-10/1/19 (net of premium)	3.80-5.00	35,965	29,340	30,654

(continued on next page)

## NOTES TO FINANCIAL STATEMENTS

Description and Due Date	Interest Rate	Original Value	2004	2003
Series 1999 Serial Bonds 4/1/03-4/1/14 (net of deferred loss on refunding of \$30)	10.00	10,285	6,343	7,163
Series 1999-CFP Serial Bonds 6/1/03-6/1/23	4.40-8.25	4,530	1,955	2,035
Series 2000-SRF Serial Bonds 10/1/03-10/1/21 (net of discount)	4.85-5.35	16,725	3,740	15,182
Series 2001-CFP Serial Bonds 6/1/03-6/1/21	4.60 - 6.00	735	660	685
Series 2001-SRF Serial Bonds 10/1/03-10/1/21 (net of discount) (net of deferred loss on refunding of \$809)	3.00 - 5.00	23,725	21,873	22,304
Series 2002-CFP Serial Bonds 6/1/03-6/1/28	3.00 - 5.60	1,700	1,545	1,605
Series 2003-CFP Serial Bonds 6/1/04-6/1/28	2.95 - 5.40	1,495	1,470	1,495
Series 2003-SRF Serial Bonds 10/1/03-10/1/23 (net of premium) (net of deferred loss on refunding of \$1,977)	2.00 - 5.00	47,250	46,687	47,492
Series 2004-CFP Serial Bonds 6/1/05-6/1/24	2.00 - 4.90	880	880	-
Series 2004-SRF Serial Bonds 10/1/05-10/1/21 (net of premium) (net of deferred loss on refunding of \$1,425)	2.00 - 4.75	11,790	10,845	-
			<u>\$ 151,160</u>	<u>\$ 158,901</u>

(continued on next page)

## NOTES TO FINANCIAL STATEMENTS

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The Bond Bank issued \$11,790 of revenue bonds (Series 2004A SRF Bonds) with an average interest rate of 4.16 percent on October 5, 2004. The net proceeds were deposited in an irrevocable trust with an escrow agent to provide for all the future debt service payments on the refunded bonds. As of December 31, 2004, \$11,005 of bonds outstanding is considered defeased and the liability has been removed from the balance sheet. The reacquisition price exceeded the net carrying amount of the old debt by \$1,446. This amount is being netted against the new debt and amortized over the life of the refunded debt, which is the same as the life of the new debt issued. This advance refunding was undertaken to reduce total debt service payments over the next 17 years by \$919 and resulted in an economic gain of \$679.

On December 16, 2003, the Bond Bank issued \$20,455 of revenue bonds (Series 2003B SRF Bonds) with an average interest rate of 4.71 percent. The net proceeds were deposited in an irrevocable trust with an escrow agent to provide for all the future debt service payments on the refunded bonds. As of December 31, 2004, \$19,740 of bonds outstanding is considered defeased and the liability has been removed from the balance sheet. The reacquisition price exceeded the net carrying amount of the old debt by \$2,129. This amount is being netted against the new debt and amortized over the life of the refunded debt, which is the same as the life of the new debt issued. This advance refunding was undertaken to reduce total debt service payments over the next 14 years by \$1,066 and resulted in an economic gain of \$842.

### NOTE 5 - ADVANCE FROM BANK OF NORTH DAKOTA

#### *Changes in Advance from Bank of North Dakota*

The following is a summary of changes in advance from the Bank of North Dakota for the year ended December 31, 2004 and 2003:

Balance, December 31, 2002	\$ 7,502
Principal payments on advance from Bank of North Dakota	(1,042)
Balance, December 31, 2003	6,460
Principal payments on advance from Bank of North Dakota	(407)
Balance, December 31, 2004	<u>\$ 6,053</u>

## NOTES TO FINANCIAL STATEMENTS

### *Maturities of Advance from Bank of North Dakota*

Maturities of principal and interest on the advance are as follows:

Years Ending December 31,	Principal	Interest	Total Debt Service
2005	\$ -	\$ 197	\$ 197
2006	31	197	228
2007	143	149	292
2008	345	181	526
2009	232	170	402
2010-2014	2,768	757	3,525
2015-2019	2,534	322	2,856
	<u>\$ 6,053</u>	<u>\$ 1,973</u>	<u>\$ 8,026</u>

### NOTE 6 - PENSION PLAN

The North Dakota Municipal Bond Bank participates in the North Dakota Public Employees' Retirement System (NDPERS) administered by the State of North Dakota. The following is a brief description of the plan.

NDPERS is a cost-sharing multiple-employer defined benefit pension plan covering substantially all classified employees of the North Dakota Municipal Bond Bank. The plan provides retirement, disability, and death benefits. If an active employee dies with less than three years of credit service, a death benefit equal to the value of the employee's accumulated contributions, plus interest, is paid to the employee's beneficiary. If the employee has earned more than three years of credited service, the surviving spouse will be entitled to a single payment refund, life-time monthly payments in an amount equal to 50% of the employee's accrued normal retirement benefit, or 60 monthly payments equal to the employee's accrued normal retirement benefit calculated as if the employee were age 65 the day before death occurred or monthly payments in an amount equal to the employee's accrued 100% joint and survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the employee's accumulated pension benefits are paid, the balance will be paid to the surviving spouse's designated beneficiary.

Eligible employees, who become totally disabled after a minimum of 180 days of service, receive monthly disability benefits that are equal to 25% of their final average salary with a minimum benefit of \$100. To qualify under this section, the employee must meet the criteria established by the Retirement Board for being considered totally disabled.

Employees are entitled to unreduced monthly pension benefits equal to 2% of their final average salary for each year of service beginning when the sum of age and years of credited service equal or exceed 85, or at normal retirement age (65). The plan permits early retirement at ages 55-64, with three or more years of service.



## NOTES TO FINANCIAL STATEMENTS

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Benefit and contribution provisions are administered in accordance with chapter 54-52 of the North Dakota Century Code. This state statute requires that 4% of the participant's salary be contributed to the plan by either the employee or by the employer under a "salary reduction" agreement. The North Dakota Municipal Bond Bank has implemented a salary reduction agreement and is currently contributing the employee's share. In addition to the 4.12% employer contribution, the employer is required to contribute 1% of each participating employee's gross wage to a prefunded retiree health insurance program. The North Dakota Municipal Bond Bank is required to contribute 4.12% of each participant's salary as the employer's share. The required contributions are determined using an entry age normal actuarial funding method. The North Dakota Retirement Board was created by the State Legislature and is the governing authority of NDPERS. The North Dakota Municipal Bond Bank's required and actual contributions to NDPERS were \$3, \$3 and \$3 for the years ended December 31, 2004, 2003, and 2002.

NDPERS issues a publicly available financial report that includes financial statements and the required supplementary information for NDPERS. That report may be obtained by writing to NDPERS; 400 East Broadway, Suite 505; P.O. Box 1657; Bismarck, ND 58502-1657.

### NOTE 7 - STATE REVOLVING LOAN FUND

Under an agreement with the North Dakota Department of Health, the Bond Bank assists in administering the State Revolving Loan Fund. The purpose of the Loan Fund is to provide low cost financing to local political subdivisions to finance wastewater disposal system projects and drinking water projects.

The federal Environmental Protection Agency (EPA) provides funds to finance approximately 80 percent of the cost of the projects. The state finances its 20 percent share of the cost through bonds issued by the Bond Bank.

As of December 31, 2004 and 2003, the following Loan Fund transactions had occurred:

	<u>2004</u>	<u>2003</u>
Municipal securities purchased	\$ 15,516	\$ 31,003
EPA grant funds received	11,414	19,250

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 8 - REBATE DUE TO IRS

Under Internal Revenue Service Code Sections 103 and 148, earnings from nonpurpose investments in excess of bond interest expense must be remitted as a rebate, once every five years, to the U.S. Treasury. A detail of the cumulative rebate at December 31, 2004 and 2003 is as follows:

	<u>2004</u>	<u>2003</u>
1993A SRF bonds	\$ 8	\$ 7
1995A SRF bonds	29	23
1996A SRF bonds	152	120
1998A SRF bonds	86	64
2000A SRF bonds	81	65
2003A SRF bonds	<u>92</u>	<u>30</u>
Rebate due to IRS	448	309
Current rebate due to IRS	<u>(110)</u>	<u>-</u>
Long-term rebate due to IRS	<u>\$ 338</u>	<u>\$ 309</u>

### NOTE 9 - RELATED PARTY TRANSACTIONS

All cash accounts of the Bond Bank are deposited in the Bank of North Dakota. All investments are under the safekeeping of the Bank of North Dakota. The Bank of North Dakota acts as paying agent for all bonds and as trustee for the 1999 Bonds and the 1993, 1995, 1996, 1998, 2000, 2001, 2003 and 2004 State Revolving Fund Bonds.

## NOTES TO FINANCIAL STATEMENTS

The Bond Bank had the following transactions with related parties summarized as follows:

	<u>2004</u>	<u>2003</u>
Bank of North Dakota		
Cash and cash equivalents - unrestricted	\$ 2,566	\$ 2,429
Cash and cash equivalents - restricted	1,602	1,781
Interest receivable	54	32
Certificates of deposit recorded as investments (current portion of \$5,549)	6,220	4,463
Advance to/from Bank of North Dakota (1)	6,053	6,460
Interest payable	16	14
Bank investment contract (2)	11,478	7,400
Expenses		
Registrar, paying agent and trustee fees	80	70
Account analysis	4	3
Information services	-	2
Letter of credit fees	9	7
Office of the Attorney General		
Legal fees	12	8
Information Technology Department		
Telecommunications and data	1	1

- (1). Notes were purchased by the Bank of North Dakota to fund required reserve funds established by the following series resolutions. The proceeds are invested in certificates of deposit with the Bank of North Dakota. Maturities and interest rates of the bonds and certificates of deposit coincide. The entire amount is noncurrent. (See Note 5).
- (2). The bank investment contract in conjunction with the SRF 2001A bond issue was awarded to the Bank of North Dakota. The investment contract is at a fixed rate and matures on October 1, 2021.

	<u>2004</u>	<u>2003</u>
CFP 1990	\$ 61	\$ 61
CFP 1991	67	67
CFP 1992	15	282
CFP 1993	1,475	1,475
CFP 1994	-	140
CFP 1995	458	458
CFP 1996	361	361
CFP 1997	2,206	2,206
1999 A/B	1,410	1,410
	<u>\$ 6,053</u>	<u>\$ 6,460</u>

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 10 - COMMITMENTS AND CONTINGENCIES

Amounts passed through from the State Department of Health from federal grantor agencies are subject to audit and adjustment by the federal grantor agencies. Any disallowed grant costs may constitute a liability. The amount, if any, of costs which may be disallowed by the grantor will be recognized in the year determined.

The Bond Bank is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. Such commitments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet.

The Bond Bank's exposure to credit loss is represented by the contractual amount of these commitments. The Bond Bank follows the same credit policies in making commitments as it does for on-balance-sheet instruments. Commitments to extend credit totaled \$41,229 and \$26,721 as of December 31, 2004 and 2003.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

On April 1, 1997, a Standby Bond Purchase Agreement was executed with the Central Dakota Irrigation District, a political subdivision. Should the District experience financial difficulties, the Bond Bank will purchase Central Dakota Irrigation District's Refunding Improvement Bonds (warrants) in an aggregate principal amount not less than the outstanding principal amount of the warrants plus accrued interest on the warrants. The original principal amount of the warrants issued April 1, 1997 was \$3,270.

The Bond Bank purchased letters of credit from the Bank of North Dakota in order to fund the reserves for the Capital Financing Program Bonds. As of December 31, 2004, \$3,315 of credit was available through these letters of credit and no funds have been advanced.

### NOTE 11 - RISK MANAGEMENT

The Bond Bank is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The following are funds/pools established by the State for risk management issues:

The 1995 Legislative Session established the Risk Management Fund (RMF), an internal service fund, to provide a self-insurance vehicle for funding the liability exposures of state agencies resulting from the elimination of the state's sovereign immunity. The RMF manages the tort liability of the state, its agencies' employees, and the University System. All state agencies participate in the RMF and their fund contribution was determined using a projected cost allocation approach. The statutory liability of the State is limited to a total of \$250 per person and \$1,000 per occurrence.

The Bond Bank also participates in the North Dakota Fire and Tornado Fund and the State Bonding Fund. The Bond Bank pays an annual premium to the Fire and Tornado Fund to cover property damage to personal property. Replacement cost coverage is provided by estimating replacement cost in consultation with the Fire and Tornado Fund. The Fire and Tornado Fund is reinsured by a third party insurance carrier for losses in excess of one million dollars per occurrence during a twelve-month period. The State Bonding Fund currently provides the Bond Bank with blanket fidelity bond coverage in the amount of \$500 for its employees. The State Bonding Fund does not currently charge any premium for this coverage.

## NOTES TO FINANCIAL STATEMENTS

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The Bond Bank, as a contributor to RMF, participates in the North Dakota Workforce Safety and Insurance (WSI), an Enterprise Fund of the State of North Dakota. WSI is a state insurance fund and a "no fault" insurance system covering the State's employers and employees financed by premiums assessed to employers. The premiums are available for the payment of claims to employees injured in the course of employment.

There have been no significant reductions in insurance coverage from the prior year and settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

**NORTH DAKOTA MUNICIPAL BOND BANK**

***SUPPLEMENTARY INFORMATION***

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**COMBINING BALANCE SHEET**  
**DECEMBER 31, 2004**  
**(In Thousands)**

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
<b>ASSETS</b>				
<b>CURRENT ASSETS</b>				
Cash and cash equivalents - unrestricted	\$ -	\$ -	\$ 2,566	\$ 2,566
Restricted				
Restricted cash and cash equivalents	245	4	1,353	1,602
Interest receivable	2,159	912	333	3,404
Investments	4,968	581	85	5,634
Municipal securities	4,863	1,428	3,238	9,529
Total restricted current assets	12,235	2,925	5,009	20,169
Total current assets	12,235	2,925	7,575	22,735
<b>NONCURRENT ASSETS - RESTRICTED</b>				
Investments	80,784	38,775	120	119,679
Municipal securities	101,534	61,420	26,738	189,692
Deferred bond financing costs, net	732	258	256	1,246
Advance to Bank of North Dakota	-	-	6,053	6,053
Total restricted noncurrent assets	183,050	100,453	33,167	316,670
Total assets	\$ 195,285	\$ 103,378	\$ 40,742	\$ 339,405
<b>LIABILITIES</b>				
<b>CURRENT LIABILITIES</b>				
Accounts payable	\$ 18	\$ 5	\$ 10	\$ 33
Rebate due to IRS	110	-	-	110
Bonds payable	4,480	1,685	2,985	9,150
Interest payable	940	426	268	1,634
Total current liabilities	5,548	2,116	3,263	10,927
<b>NONCURRENT LIABILITIES</b>				
Rebate due to IRS	199	139	-	338
Bonds payable, net	75,057	39,480	27,474	142,011
Advance from Bank of North Dakota	-	-	6,053	6,053
Total noncurrent liabilities	75,256	39,619	33,527	148,402
Total liabilities	80,804	41,735	36,790	159,329
<b>NET ASSETS</b>				
Unrestricted	-	-	2,556	2,556
Restricted for debt service	55,172	33,169	1,396	89,737
Restricted for loan purposes	59,309	28,474	-	87,783
Total net assets	114,481	61,643	3,952	180,076
Total liabilities and net assets	\$ 195,285	\$ 103,378	\$ 40,742	\$ 339,405

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS**  
**YEAR ENDED DECEMBER 31, 2004**  
**(In Thousands)**

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
<b>OPERATING REVENUES</b>				
Investment income	\$ 2,739	\$ 1,416	\$ 1,965	\$ 6,120
Administrative fees and other	535	263	118	916
	<u>3,274</u>	<u>1,679</u>	<u>2,083</u>	<u>7,036</u>
<b>OPERATING EXPENSES</b>				
Interest expense	4,153	1,678	2,095	7,926
State Revolving Fund administration	452	36	-	488
State Revolving Fund set-asides	-	395	-	395
Rebate due to IRS	67	70	-	137
Salaries and benefits	-	-	112	112
Amortization of bond issue costs	87	24	42	153
Operating	-	-	31	31
Paying agent fees	-	-	9	9
	<u>4,759</u>	<u>2,203</u>	<u>2,289</u>	<u>9,251</u>
<b>OPERATING LOSS</b>	<u>(1,485)</u>	<u>(524)</u>	<u>(206)</u>	<u>(2,215)</u>
<b>NONOPERATING REVENUE</b>				
Grant and set-asides	3,344	8,070	-	11,414
Investment income	5,350	1,819	312	7,481
	<u>8,694</u>	<u>9,889</u>	<u>312</u>	<u>18,895</u>
<b>INCOME BEFORE TRANSFERS</b>	7,209	9,365	106	16,680
<b>TRANSFERS</b>	<u>(2,645)</u>	<u>2,645</u>	<u>-</u>	<u>-</u>
<b>CHANGE IN NET ASSETS</b>	4,564	12,010	106	16,680
<b>TOTAL NET ASSETS, BEGINNING OF YEAR</b>	<u>109,917</u>	<u>49,633</u>	<u>3,846</u>	<u>163,396</u>
<b>TOTAL NET ASSETS, END OF YEAR</b>	<u>\$ 114,481</u>	<u>\$ 61,643</u>	<u>\$ 3,952</u>	<u>\$ 180,076</u>



**NORTH DAKOTA MUNICIPAL BOND BANK**  
**COMBINING STATEMENT OF CASH FLOWS**  
**YEAR ENDED DECEMBER 31, 2004**  
**(In Thousands)**

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
<b>OPERATING ACTIVITIES</b>				
Receipts of administrative fees from customers	\$ 536	\$ 263	\$ 118	\$ 917
Payments to service providers	(485)	(430)	(37)	(952)
Payments to employees	-	-	(112)	(112)
Payment of rebate to IRS	-	-	-	-
<b>NET CASH FROM (USED FOR) OPERATING ACTIVITIES</b>	<b>51</b>	<b>(167)</b>	<b>(31)</b>	<b>(147)</b>
<b>NONCAPITAL FINANCING ACTIVITIES</b>				
Grant and set-asides	3,344	8,070	-	11,414
Transfers	(2,645)	2,645	-	-
Interest paid on bonds payable	(3,728)	(1,750)	(2,066)	(7,544)
Bond financing costs	(124)	-	-	(124)
Principal payment on advance from Bank of North Dakota	-	-	(407)	(407)
Proceeds from bond premiums	509	-	-	509
Proceeds from issuance of bonds payable	11,790	-	880	12,670
Principal payments on bonds payable	(16,766)	(1,180)	(3,160)	(21,106)
<b>NET CASH FROM (USED FOR) NONCAPITAL FINANCING ACTIVITIES</b>	<b>(7,620)</b>	<b>7,785</b>	<b>(4,753)</b>	<b>(4,588)</b>
<b>INVESTING ACTIVITIES</b>				
Interest received on investments and municipal securities	8,087	3,155	2,309	13,551
Collection of advance to Bank of North Dakota	-	-	407	407
Proceeds from maturities and sales of investments	20,810	16,181	1,818	38,809
Purchases of investments	(25,027)	(17,323)	(1,738)	(44,088)
Proceeds from maturities of municipal securities	6,583	2,878	2,955	12,416
Purchases of municipal securities	(3,006)	(12,509)	(887)	(16,402)
<b>NET CASH FROM (USED FOR) INVESTING ACTIVITIES</b>	<b>7,447</b>	<b>(7,618)</b>	<b>4,864</b>	<b>4,693</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(122)</b>	<b>-</b>	<b>80</b>	<b>(42)</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<b>367</b>	<b>4</b>	<b>3,839</b>	<b>4,210</b>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ 245</b>	<b>\$ 4</b>	<b>\$ 3,919</b>	<b>\$ 4,168</b>

(continued on next page)

# COMBINING STATEMENT OF CASH FLOWS – Page 2

	Clean Water SRF	Drinking Water SRF	Capital Financing Program	Total
RECONCILIATION OF OPERATING LOSS TO NET CASH USED FOR OPERATING ACTIVITIES				
Operating loss	\$ (1,485)	\$ (524)	\$ (206)	\$ (2,215)
Adjustments to reconcile operating loss to net cash used for operating activities				
Amortization of bond financing costs	87	24	42	153
Net amortization (accretion) of premium (discount) on bonds payable	(741)	(61)	52	(750)
Reclassification of investment income and expense to other activities	2,155	321	78	2,554
Changes in assets and liabilities				
Accounts payable	(33)	2	3	(28)
Rebate due IRS	68	71	-	139
NET CASH FROM (USED FOR) OPERATING ACTIVITIES	<u>\$ 51</u>	<u>\$ (167)</u>	<u>\$ (31)</u>	<u>\$ (147)</u>

**NORTH DAKOTA MUNICIPAL BOND BANK**  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
**YEAR ENDED DECEMBER 31, 2004**

**EXHIBIT A-1**

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures (In Thousands)</u>
<b>ENVIRONMENTAL PROTECTION AGENCY</b>		
Passed Through the North Dakota Department of Health		
Capitalization Grants for State Revolving Funds	66.458	\$ 3,344
Capitalization Grants for Drinking Water State Revolving Funds	66.468	8,038
State Grants to Reimburse Operators of Small Water Systems for Training and Certification Costs	66.471	<u>32</u>
Total Environmental Protection Agency		<u>\$ 11,414</u>

**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES**

The accompanying schedule of expenditures of federal awards is presented on the accrual basis of accounting.

**NOTE 2 - AGENCY OR PASS-THROUGH NUMBER**

The pass-through entity has not provided us with the identifying number on all programs, therefore, they are not included in this schedule.

**NOTE 3 - SUBRECIPIENTS**

Of the federal expenditures presented in the schedule, the North Dakota Municipal Bond Bank provided federal awards to subrecipients as follows:

<u>Program Title</u>	<u>Federal CFDA Number</u>	<u>(In Thousands)</u>
Capitalization Grants for State Revolving Funds	66.458	\$ 2,971
Capitalization Grants for Drinking Water State Revolving Funds	66.468	7,883
State Grants to Reimburse Operators of Small Water Systems for Training and Certification Costs	66.471	<u>32</u>
		<u>\$ 10,886</u>

The above awards consist entirely of loans advanced to the subrecipients.

The North Dakota Municipal Bond Bank also has outstanding loan balances to subrecipients from prior years. These balances are not included on the accompanying schedule of expenditures and federal awards because the federal government imposes no continuing compliance requirements on the subrecipient.

**NORTH DAKOTA MUNICIPAL BOND BANK  
SUMMARY SCHEDULE OF PRIOR FEDERAL AUDIT FINDINGS  
YEAR ENDED DECEMBER 31, 2004**

**EXHIBIT A-2**

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**2003-2:** Grant: CFDA #66.468 State Revolving Loan Program – Drinking Water, Grant Year December 31, 2003,  
Questioned Costs: None

*Statement of Condition*

The State Revolving Loan Program – Drinking Water requires annual financial status reports to be submitted. The North Dakota Municipal Bond Bank and North Dakota Department of Health did not submit the required annual report for the year ended December 31, 2002.

*Recommendation*

We recommend the North Dakota Municipal Bond Bank oversee the submission of the required report for the year ended December 31, 2002. We also recommend the North Dakota Municipal Bond Bank review the procedures with the North Dakota Department of Health relating to the required Drinking Water reports to ensure all required reports are timely filed.

*Response*

The North Dakota Municipal Bond Bank and North Dakota Department of Health have completed and filed the 2002 Drinking Water financial status reports. In the future, the Drinking Water financial status reports will be filed annually.

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE  
AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED  
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

We have audited the basic financial statements of **North Dakota Municipal Bond Bank**, a component unit of the State of North Dakota, as of and for the year ended December 31, 2004 and have issued our report thereon dated January 26, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

*Internal Control over Financial Reporting*

In planning and performing our audit, we considered **North Dakota Municipal Bond Bank's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect **North Dakota Municipal Bond Bank's** ability to record, process, summarize and report financial data consistent with the assertions of management in the basic financial statements. The reportable condition is described in the accompanying schedule of findings and questioned costs as 2004-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all reportable conditions that also considered to be material weaknesses. However, we believe the reportable condition described above is not a material weakness.

*Compliance and Other Matters*

As part of obtaining reasonable assurance about whether **North Dakota Municipal Bond Bank's** basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.

*Eide Bailly LLP*

Bismarck, North Dakota  
January 26, 2005

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS  
APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL  
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

*Compliance*

We have audited the compliance of **North Dakota Municipal Bond Bank** with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended December 31, 2004. **North Dakota Municipal Bond Bank's** major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of **North Dakota Municipal Bond Bank's** management. Our responsibility is to express an opinion on **North Dakota Municipal Bond Bank's** compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about **North Dakota Municipal Bond Bank's** compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on **North Dakota Municipal Bond Bank's** compliance with those requirements.

In our opinion, **North Dakota Municipal Bond Bank** complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2004.

*Internal Control Over Compliance*

The management of **North Dakota Municipal Bond Bank** is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered **North Dakota Municipal Bond Bank's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.

*Eide Bailly LLP*

Bismarck, North Dakota  
January 26, 2005



**NORTH DAKOTA MUNICIPAL BOND BANK  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
YEAR ENDED DECEMBER 31, 2004**

**EXHIBIT A-5**

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**A. SUMMARY OF AUDIT RESULTS**

1. The auditor's report expresses an unqualified opinion on the financial statements of the North Dakota Municipal Bond Bank.
2. A reportable condition in internal control was disclosed by the audit of the financial statements. This reportable condition is not considered to be a material weakness.
3. No instances of noncompliance material to the financial statements of the North Dakota Municipal Bond Bank which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. The auditor's report on compliance for the major federal award program for the North Dakota Municipal Bond Bank expresses an unqualified opinion on the major federal program.
5. There were no audit findings relative to the major federal award program for the North Dakota Municipal Bond Bank.
6. The program tested as a major program was #66.458 State Revolving Loan Program – Clean Water.
7. The threshold for distinguishing a Type A program was \$342,000.
8. The North Dakota Municipal Bond Bank was determined to be a low-risk auditee.

**B. FINDINGS - FINANCIAL STATEMENT AUDIT**

**2004-1**

*Statement of Condition*

Accounting personnel is responsible for cash receipts, cash disbursements and maintaining the financial reporting system.

*Criteria*

Segregation of accounting functions necessary to assure adequate internal control.

*Recommendation*

This is not unusual in organizations of this size, but the Commission should be constantly aware of this condition and realize that the concentration of duties and the responsibilities in a limited number of individuals is not desirable from a control point of view. Under these conditions, the most effective controls lie in the Commission's knowledge of matters relating to the North Dakota Municipal Bank's operations.

*Current Status*

Management has addressed the segregation of accounting issue that comes with the small office of the North Dakota Municipal Bond Bank. Management is working with the Bank of North Dakota to implement additional internal control procedures. With this in mind, procedures have been and will continue to be implemented to provide the highest level of internal control possible.

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**C. FINDINGS – MAJOR FEDERAL AWARD PROGRAM AUDIT**

None.

**NORTH DAKOTA MUNICIPAL BOND BANK  
INDEPENDENT AUDITOR'S SPECIFIC COMMENTS REQUESTED BY THE  
NORTH DAKOTA LEGISLATIVE AUDIT AND FISCAL REVIEW COMMITTEE  
YEAR ENDED DECEMBER 31, 2004**

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The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

The Legislative Audit and Fiscal Review Committee requires that certain items be addressed by independent certified public accountants performing audits of state agencies. The items and our responses are as follows:

1. Were expenditures made in accordance with legislative appropriations and other state fiscal requirements and restrictions?

Yes.

2. Were revenues accounted for properly?

Yes.

3. Were there adequate financial controls and procedures?

Yes.

4. Was there an adequate and effective system of internal control?

The limited number of office personnel prevents a proper segregation of accounting functions necessary to ensure adequate internal control.

In conjunction therewith, see the reportable condition on internal control in the Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*.

5. Do financial records and reports reconcile with those of state fiscal offices?

Based on our audit procedures, financial records and reports reconciled to data maintained by the Office of Management and Budget.

6. Was there compliance with statutes, laws, rules and regulations under which the Agency was created and is functioning?

Yes.

7. Was there any indication of fraud or dishonesty?

No.

8. Were there any indications of lack of efficiency in financial operations and management?

No.

9. Was action taken on prior audit findings and recommendations?

Management has addressed the segregation of accounting issue that comes with the small office of the North Dakota Municipal Bond Bank. Management is working with the Bank of North Dakota to implement additional internal control procedures. With this in mind, procedures have been and will continue to be implemented to provide the highest level of internal control possible.

10. Were all activities of the agency encompassed within appropriations of specific amounts?

All general operating activities are encompassed by appropriations. All other activities are exempt from State appropriations.

11. Has the Agency implemented the statewide accounting and management information system including the cost allocation system?

No. The North Dakota Municipal Bond Bank has their own accounting system. The uniqueness of the Bond Bank's accounting and management information needs require the Bond Bank to utilize other software systems.

12. Has the Agency developed budgets of actual anticipated expenditures and revenues on at least a quarterly basis and compared on at least a quarterly basis actual expenditures and revenues on the accrual basis to budgeted expenditures and revenues?

No, the Bond Bank has not adopted a formalized budget to actual expenditures due to the fact that not all of their revenue/expenditures fall under a legislative appropriation. However, the Bond Bank does monitor the funds appropriated through the Industrial Commission and our review of the Bond Bank's procedures indicated adequate controls.

This report is intended solely for the information and use of the North Dakota Industrial Commission, Legislative Audit and Fiscal Review Committee, management, and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.

*Eide Bailly LLP*

Bismarck, North Dakota  
January 26, 2005